

## ABC Oil Industries Private Limited

### Ratings

Facilities	Amount (Rs. in Million)	Ratings <sup>1</sup>	Rating Action
Long Term Bank Facilities	260.71	CARE-NP BB- [Double B Minus]	Reaffirmed
Short Term Bank Facilities	730.00	CARE-NP A4 [A Four]	Reaffirmed
Total Facilities	990.71 (Nine Hundred Ninety Million Seven Hundred and Ten Thousand Only)		

*Details of Facilities in Annexure 1*

Care Ratings Nepal Limited (CRNL) has reaffirmed the rating of 'CARE-NP BB-' assigned to the long-term bank facilities and the rating of 'CARE-NP A4' assigned to the short-term bank facilities of ABC Oil Industries Private Limited (ABC).

### Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of ABC continue to remain constrained by the company's limited track record of operations along with ABC's reliance on exports to India for a significant portion of its income, which is dependent on benefits derived from South Asian Free Trade Area (SAFTA) agreement. The company's prospects of ramping up its scale going forward remains impacted due to change in the duty structure of importing country (India) for exports from Nepal. The ratings also factor in working capital-intensive nature of business, leveraged capital structure, raw materials price volatility risk, foreign exchange fluctuation risk, exposure to regulatory risk, and competitive nature of industry.

The ratings, however, continue to derive strengths from experienced promoters and management team, locational advantage for both imports and exports, and stable demand prospects for edible oils over the medium term, which however, is offset to some extent by the volatility in export opportunities for Nepalese refiners.

*Going forward, the ability of the company to manage growth in operations while improving profit margins, rationalize its debt through efficient working capital management, and pass through changes in raw material prices to the customers while managing the foreign exchange fluctuation risks will be the key rating sensitivities. Furthermore, any change in the regulatory framework pertaining to trade regulations and tariff differential with India impacting exports prospects will also be a key rating sensitivity.*

### Detailed Description of the Key Rating Drivers

#### Key Rating Weaknesses

#### Short track record of operations and operational stabilization risk in initial years of operations

ABC started its commercial operations from mid-May 2022 and has a relatively short track record of operations as compared to other established players. During its first full year of operations in FY23, ABC generated a total operating income (TOI) of Rs. 2,127 Mn via sales of refined palm oil, sunflower oil, and soybean oil etc. The TOI was lower than earlier envisaged owing to lower exports to India. Exports to India continues to be impacted by reduced scope for arbitrage following the introduction of 5% import duty on all crude oils- crude palm oil, sunflower oil, and soybean oil and lowering of import duty on refined sunflower oil and soybean oil from 17.5% to 12.5 % by Government of India (GoI) in June 15, 2023 to help curb exorbitantly high oil prices in India. Until a positive revision in the import duty by GoI, exports prospects for ABC remain slim, likely leading to muted income levels over the near-term. PBILDT margin of 7.61%, the company reported PAT of Rs. 52 Mn, and gross cash accrual (GCA) of Rs. 97 Mn during FY23. Capacity utilization was low at 18.16% during FY23. Stabilization of operations amid a challenging operating environment remains critical from analytical perspective.

<sup>1</sup>Complete definitions of the ratings assigned are available at [www.careratingsnepal.com](http://www.careratingsnepal.com) and in other CRNL publications.

**Working capital intensive nature of business**

ABC's operations are working capital intensive in nature as the company imports raw materials from various countries such as Indonesia, Malaysia, Russia, Ukraine etc. through opening of Letter of Credit (LC). The company needs to keep enough inventory for smooth operations which leads to high reliance on working capital borrowings. Lead time for procurement of crude palm oil is up to one month, whereas lead time for soybean and sunflower oil is up to three months. With an average collection period of 47 days, average inventory period of 40 days, and average creditor period of 9 days, the operating cycle of ABC stood at 78 days in FY23. Average utilization of both fund-based and non-fund based working capital limits stood ~80% during the last twelve-month period ended mid-October.

**Leveraged capital structure with moderate debt coverage indicators**

The capital structure of the company remained leveraged with overall gearing of 2.70x, and total debt/GCA of 9.17x at the end of FY23. ABC's coverage indicator stood moderate with an interest coverage ratio of 2.27x in FY23. Going forward, to cater growth in scale of operations, which are working capital intensive in nature, the company might need to further increase its reliance on the bank borrowings for working capital requirements. The company's ability to rationalize debt levels leading to improved gearing headroom will be critical from credit perspective.

**Raw material price volatility risk and foreign exchange fluctuation risk**

ABC's major raw materials include crude palm oil, crude soybean oil, and crude sunflower oil and are imported from aforementioned countries. The prices of ABC's raw materials are market linked and determined on a periodic basis, thus exposing the company to the volatility in the prices of raw materials which has a bearing on its profitability margins. The raw materials cost contributed around 80% of the total operating income during FY23. Furthermore, the total raw material requirement is met through imports and the prices of the same are linked to USD, for which the company is exposed to the foreign exchange fluctuation risk. The ability of the company to pass through changes in raw material prices to the customers and manage the foreign exchange fluctuation risks related to raw materials will be crucial from its profitability perspective.

**Exposure to regulatory risk**

The operations of ABC are vulnerable to regulatory risk arising from various laws and policies of importing and exporting countries coupled with the domestic policies of Nepal. ABC's exports revenue relies on the tariff arbitrage in India between direct imports of crude by Indian millers vis-à-vis imports of refined edible oil from Nepal. ABC, like many millers in Nepal, try to exploit any substantial tariff differential in India, which keep changing for different edible oils every year. Over the past few years, there have been changes in government policies, either domestic or international regarding import/export of edible crude. ABC's revenue is susceptible to regulatory policies relating to tariff barriers (differential trade tariffs among South Asian Free Trade Area), non-tariffs barriers (restriction on the quality of imports), international freight rates etc. Any sustained unfavorable change in policies by local governments could impact the export of refined oils or procurement of crude oils and could have a bearing on the financial profiles refiners like ABC.

**Fragmented and Competitive nature of industry**

Import and processing/refining of edible oils is highly fragmented due to presence of several organized/ unorganized players owing to low entry barrier and low technology and capital requirement. Low product differentiation of ABC's product results in high competition from other players including traders. Considering the competitive nature of industry, the millers have low pricing power. Agro products are also seasonal in nature with production dependent on various factors such as monsoon and climatic condition, exposing the fate of the company's operation to vagaries of nature.

**Key Rating Strengths****Experienced promoters and management team**

The company is managed under the overall guidance of its five-member Board of Directors (BoD) which includes experienced businessmen/industrialists with long experience in various sectors. Mr. Sanjay Koirala, the company's Chairman, has an experience of more than two decades in industrial sector of Nepal, which includes trading of oil, manufacturing of soap and packaging materials. He is also an advocate under Nepal Bar Council. Other directors also have up to ten years of experience ranging from trading and manufacturing to financial sectors. The board is aptly supported by experienced management team across various departments.

**Locational advantage for both imports and exports**

The manufacturing facility of the company is located in Duhabi, Sunsari district which is around 13 km from Jogbani, a major custom point between India and Nepal. Since all of the raw materials requirements of ABC imported from various countries are unloaded on Indian ports, the factory's proximity to the border leads to savings in freight cost. Close proximity to Indian border is also beneficial from the company's export perspective as ~74% of its revenue was derived through exports to India in FY23.

**Essential part of cooking leading to stable demand prospects**

ABC is involved in processing/refining of crude oils into refined oils. The demand prospect of oil industry is growing as oil is one of essential commodity for cooking. Furthermore, with demand being higher than domestic production and slowdown in domestic agriculture production, large volume of edible as well as crude oil is being imported in Nepal giving importers like ABC a favourable business environment.

**Industry Outlook**

Amid changes in duty structure (lower/zero import duty) by Government of India (GoI) on imports of various crude edible oils, Nepalese refiners' income levels in FY23 have dropped substantially compared to the high growths reported over FY21-FY22 which was supported by surging exports to India of palm olein and soybean oil. According to Department of Customs and the Trade and Export Promotion Center (TEPC), export of palm oil to India from Nepal has declined by 50.1% on a year-on-year (y-o-y) basis in FY23. Likewise, export of soybean oil has reduced by 82.4%, and that of sunflower oil has reduced by 90.2% on a year-on-year (y-o-y) basis in FY23. While there maybe future potential for Nepalese refiners in case of upward revision in import duty of various edible oils in India, for the time being, operating environment for refiners like ABC are likely to remain impacted over the near term as export opportunities to India remain slim. Nonetheless, exports will remain contingent upon the intermittent changes in related policies of GoI, resulting in a volatile income level for refiners like ABC going forward as well.

**About the Company**

ABC Oil Industries Private Limited (ABC) was incorporated on July 25, 2021 for processing/refining of edible oils, and has manufacturing facility in Duhabi, Sunsari, Nepal. The company commenced its operations from May 15, 2022. The total installed capacity of the plant is 60,000 Metric Tons Per Annum (MTPA) that includes 36,000 MTPA capacity for refining of crude palm oil, and 12,000 MTPA capacity each for refining of Soybean Oil and Sunflower Oil.

**Brief Financials of the company**

(Rs. In Mn)

Particulars	FY22 (A)	FY23 (UA)
Income from Operations	237	2,127
PBILDT Margin (%)	4.44	7.61
Overall Gearing (times)	3.03	2.70
Interest Coverage (times)	3.21	2.27
Current Ratio (times)	0.93	1.22
Total Debt/Gross Cash Accruals (times)	72.69	9.17

(A): Audited, (UA): Unaudited

**Annexure 1: Details of the Facilities rated**

Nature of the Facility	Type of the Facility	Amount (Rs. in Million)	Rating
Long Term Bank Facilities	Fixed Term Loan	260.71	CARE-NP BB- [Double B Minus]
Short Term Bank Facilities	Fund Based/ Non-Fund Based Limits	730.00	CARE-NP A4 [A Four]
<b>Total</b>		<b>990.71</b>	

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